Research on China's Fdi Risks and Avoidance Strategies in Countries Along the "Belt and Road"

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Abstract: Along with the gradual advancement of the "Belt and Road" process, the initiative creates good opportunities for China's "going out" strategy and will also leave a strong mark on the economic development history of many countries along the route. In recent years, China's "Belt and Road" direct investment in railway lines has entered a rapid development stage, diverging some countries and industries, and greatly promoting the development of our country and the countries along the route. On the basis of summarizing the status of China's direct investment in countries along the "Belt and Road", this article analyzes the risks of Chinese enterprises FDI from the four aspects of sovereign credit, politics, economy, and culture. And then further provide recommendations in terms of prevention of exogenous risks, prevention of currency and financial risks, and governance of enterprise endogenous risks..

1. Introduction

1.1 Investment Scale

From 2013 to 2019, China has cumulatively invested US $179.47 billion in direct investment in countries along the "Belt and Road", and established more than 10,000 overseas companies in countries along the route[1].

Regarding the flow, as shown in Figure 1-1, the flow of China's FDI in countries along the "Belt and Road" is becoming more volatile. It has been increasing year by year since 2013 and peaked in 2017. As of the end of 2019, direct investment flow reached US $18.69 billion, up 4.5% year-on-year, accounting for 13.7% of China's FDI flow during the corresponding period.

Regarding the stock, as shown in Figure 1-2, China's FDI stock in countries along the route are steadily increasing. Up to the end of 2019, the total investment scale amounted to US $179.47 billion, accounting for 8.2% of all foreign investment stocks in China, which is nearly twice as high as in 2013.

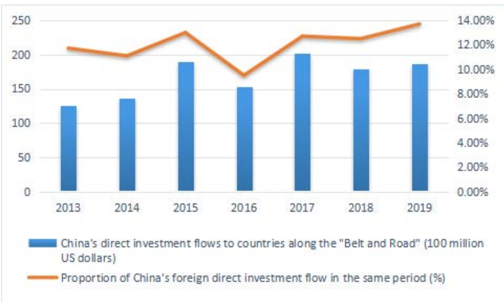

Fig.1 2013-2019 China's Fdi Flow in Countries Along the "Belt and Road" and Its Proportion in the Same Period

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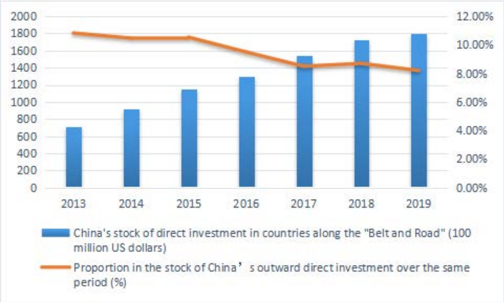

Fig.2 2013-2019 China's Fdi Stock in Countries Along the "Belt and Road" and Its Proportion in the Same Period

1.2 Regional Distribution

The "Belt and Road" economic belt, as the economic corridor with the longest span and the best development potential today, spans Eurasia, the Western Pacific and the Indian Ocean, radiates 64 countries and covers a wide range of regions[2].

On a national scale, China's "Belt and Road" FDI stock is highest in Singapore, Indonesia, Russia, Laos and Malaysia. According to data, China's "Belt and Road" FDI stock in the top 10 countries accounts for about 73% of total direct investment along the route. This indicates that China's FDI is concentrated in neighboring countries close to China.

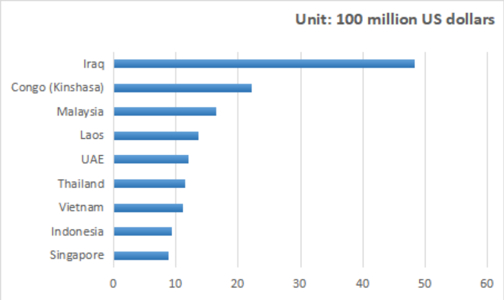

Fig.3 The Top Ten Countries Ranked by China's Fdi Flows to Countries Along the "Belt and Road" in 2019

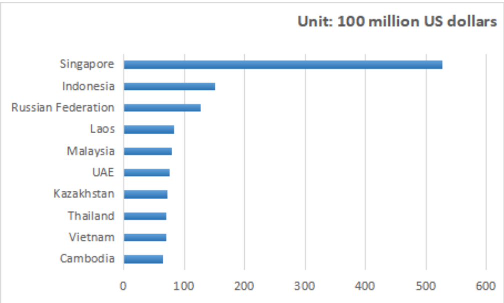

Fig.4 As of 2019, China's Top Ten Countries in the Stock of Fdi in Countries Along the "Belt and Road"

From the regional level, Southeast Asia is the largest investment scale, with a direct investment scale of US $102.638 billion, followed by Mongolia Russia, West Asia, Central Asia and South Asia, and the direct investment in these four area has been a major reversal in the last decade. China is relatively low in FDI share to Central and Eastern Europe and its growth rate has been slow.

From the perspective of various economic types, China's FDI in states along the route is predominantly focused on developing countries, and the average percentage of is about 75% in the past 10 years. China's FDI in the surrounding developed economies has always accounted for a small proportion, while FDI for transition economies is stable.

1.3 Industry Distribution

The industry distribution of China's FDI in countries along the "Belt and Road" has changed in different periods, showing a diversified trend. As of 2019,the energy industry is no longer dominant, with leasing and business services, wholesale and retail, and financial industry attracting more investment. China's FDI spans all sectors of the national economy, and there are 6 industries with a stock scale of over US $100 billion.

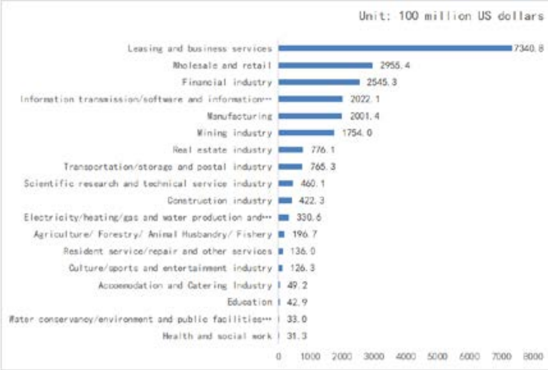

Fig.5 Industry Distribution of China's Fdi Stock At the End of 2019

1.4 Distribution of Investment Entities

Since the "Belt and Road" initiative was put forward, the proportion of non-state-owned enterprises has tended to fluctuate, the overall change is small, and state-owned enterprises still take over a core position. Of the amount of non-financial FDI at the end of 2019, the amount of investment by state-owned enterprises was approximately US $991.619 billion, accounting for 50.1%.And the investment amount of non-state-owned enterprises was about US $970.231,accounting for 49.9%.Among them, the non-state-owned enterprises that invest directly along "Belt and Road" are mostly in developed eastern areas such as Beijing, Shanghai, and Guangzhou, and the western and central inland areas are significantly lower than the eastern areas. The financial direct investment subjects are relatively concentrated and are currently basically monopolized by state-owned financial enterprises representing the four major state-owned banks. At the end of 2019,the financial investment flow was US $199.5 billion, and the stock was US $254.53 billion.

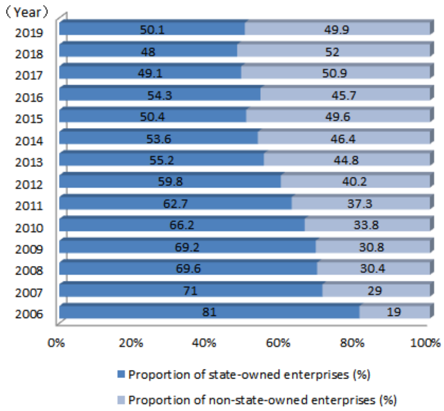

Fig. 1 the Proportion of the Stock of State-Owned and Non-State-Owned Enterprises in China from 2006 to 2019

2. Risk Analysis of China's Fdi in Countries Along the Belt and Road

2.1 Sovereign Credit Risk

Most of the countries along the route are Asian countries, whose investment and financing environment is less than that of Europe, America and China. Therefore, China's FDI in its short-term prospects are not optimistic, and some of them are likely to become bad debts, facing the risk of debt default from the invested countries. According to Moody's assessment report,42 major countries along the route have credit ratings below investment grade, or even outside the rating range, which means the potential credit risk is high. The relevant data in Table 2-1 shows the total amount of failed or blocked investment by Chinese companies in the countries along the route from 2006 to 2016. The total amount involved was US $52.62 billion, which occurred in 20 countries.

Table 1 Statistics of Fdi Risk Cases of Chinese Enterprises from 2006 to 2016

Years	Number of cases	Amount /100 million US dollars
2006	6	218.7
2007	5	73.6
2008	1	3
2009	2	18.3
2010	4	18.3
2011	2	40.5
2012	6	86.4
2013	4	69.5
2014	10	149.4
2015	7	76.9
2016	2	22.6

2.2 The Risks of Political

2.2.1 The Risk of Political Unrest in the Host Country

"Belt and Road" covers a wide scope of geographically complex relationships along the route, and more than half of the countries have an extremely bad investment environment. Moreover, terrorist forces are rampant along the Belt and Road and have formed an arc-shaped terrorist zone of "West Asia, Middle East-South Asia-Central Asia", with terrorist attacks and wars against terrorism occurring one after another[3]. At the same time, the competing game between major powers and the intertwining of many powerful forces have increased the uncertainty in the increase of FDI by Chinese enterprises.

2.2.2 The Risk of Host Country Policy Changes

The policy of the host country has changed from time to time, lacking a certain degree of continuity. The governments may change some domestic policies on the grounds of public interest and environmental protection, and withdraw the preferential conditions given to China or even make foreign investors' projects forced to stop, seriously damaging their legitimate property rights and interests.

2.3 The Risks of the Economy

2.3.1 Macroeconomic Risks

The economic growth of the regions along the Belt and Road is generally better than the global average, and it is one of the regions with the most economic growth potential in the world. Central and Eastern Europe, Southeast Asia and some CIS countries have a good industrial base; the Middle East, Central Asia and Russia are rich in energy and mining resources; South Asian countries have superior labor resources; the Middle East and Southeast Asia have a high degree of financial deepening, which makes the strong economic complementarity between the regions.

2.3.2 Financial Risks

Countries along the "Belt and Road" usually have relatively small foreign exchange reserves, so that foreign exchange market price is linked and exchange rate fluctuations are difficult to predict. China's investment will face multiple exchange rate risks such as rising investment costs and exchange losses brought about by the changing investment and financing environment. Interest rate risk and inflation risk are also financial risks that cannot be ignored. Many countries along the route have serious inflation problems.

2.4 The Risks of Cultural

2.4.1 Great Cultural Differences and Intense Religious Conflicts

The countries along the “Belt and Road” basically cover all regions of four ancient civilizations, and languages, social habits, historical customs, religious beliefs and other aspects of each country show diversified characteristics. Under this difference, the lack of understanding of local culture will also lead to misjudgments of Chinese companies' foreign investment, violate the cultural concepts of local residents, cause conflicts, and hinder construction and development.

2.4.2 Deliberate Incitement by Major Countries and Fermentation of Anti-Chinese Sentiment

In recent years, some unsuspecting countries have made statements such as China threat theory and taken a series of related measures to contain China's development. They misinterpreted the “Belt and Road Initiative” as a Chinese version of the “Marshall Plan”, and have used political dialogue, economic and military threats to pressure countries interested in participating in it[4]. Misled by these malicious statements, some countries along the route have developed anti-China sentiments that continue to fester, and these countries are likely to oppose and undermine China's FDI projects under the guidance of misguided public opinion.

3. Policy Recommendations to Deal with the Fdi Risks of Countries Along the “Belt and Road”

3.1 Build a Risk Early Warning System and Sign a Bilateral Investment Agreement

First, before making FDI in countries along the “Belt and Road”, information asymmetry ought to be reduced as much as possible. For one thing, we should grasp the rating status of various indicators of these countries by international institutions in advance, and collect relevant information about the host country extensively and accurately. For another, the Chinese government should develop a complete information collection and analysis system, such as cooperation with the government's purchasing and internationally existing data systems, to establish an overseas investment risk assessment index, and make a risk warning to China's foreign direct investment firms.

Second, China should continue to actively sign and upgrade bilateral or multilateral investment agreements with countries along the route, stipulate treatment standards, investment projects and the contents of foreign investors[5]. And pay attention to the standardization of terms in order to ensure the long-term stability of the investment policy of the host country.

3.2 Consummate Insurance Protection Measures and Strengthen Industry Management and Supervision

In recent years, Chinese enterprises' FDI in countries around the “Belt and Road” has revealed diversified, large-scale, and innovative features, and most of the countries along the route are high-risk countries. Therefore, it’s necessary to improve the insurance safeguard for Chinese FDI so that the losses suffered in the process can be remedied.

On the one hand, it’s necessary to establish and perfect the overseas investment insurance system for enterprises, increase the insurance scope and amount, effectively safeguard the interests of Chinese investors and ensure the stability and health of international cooperation. For another, strengthen the management and supervision of industry associations, effectively play the role of industry associations as a bridgehead for industry self-discipline, and build a great overseas business circumstance through comprehensive use of access threshold, technical standards,quality supervision and other means, and avoid industry disorder and make up for the deficiencies of the government in overseas asset management[6].

3.3 Consummate the Financial Support System and Optimize the Investment Industry Layout

For the prevention of economic risks, first of all, China should perfect the financial support system for FDI with the state as the pillar, professional institutions and organizations as the main body, and adequate participation of social capital. Pay attention to the changes in exchange rates, interest rates and inflation rates, and systematically analyze the economic operation of countries along the “Belt and Road”, and assists the government to help companies preferentially choosing countries with stable economic operations and high credit ratings for investment.

Second, Chinese enterprises should do a good job in research, comprehensive analysis, and local conditions, make a differentiated direct investment model and project selection, make a “risk-return” balance, evaluate their own risk tolerance[7], and plan carefully when investing abroad. Investment distribution, avoid situations where the return is far less than expected due to unfamiliarity with the economic conditions and investment environment of the host country.

3.4 Respect the Cultural Differences of Various Countries and Promote People-to-People Exchanges across the World

First, Chinese companies should be deeply aware of the languages, religion and customs of the countries around the route, recognize and respect cultural differences, strengthen exchanges with local cultures, get the recognition of local people, and show the inclusiveness and openness of culture.

Second, “People to people connection” is a momentous section of building” connectivity “Belt and Road”. China should seize the opportunities such as International Cooperation Summit Forum and clarify the connotation of the “Belt and Road Initiative”, and promote all countries to reach a consensus on building a community with a shared future for mankind.

Third, adopt the “localization strategy” and integrate into the host society management system. Chinese enterprises should dilute the color of parent company, carry out localization strategies regarding staff, raw materials and technology development, and abide by local laws and regulations.

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